UNITED NATIONS

ECONOMIC AND SOCIAL COUNCIL

Distr.

LIMITED
E/ECA/TRADE/90/25
December 1990

Original: ENGLISH

ECONOMIC COMMISSION FOR AFRICA

Conference of African Ministers
of Trade, Eleventh Session

15 - 19 April 1991

Addis Ababa, Ethiopia

REPORT ON THE IMPACT OF UNRECORDED TRANSBORDER TRADE IN THE INFORMAL SECTOR

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I. INTRODUCTION

1. African countries inherited political rather than historical boundaries from the former colonial powers. In many cases, these boundaries cut across ethnic groups, cultures, traditions, style of living, languages and systems. However, this artificial division has not prevented some of the African people who live alongside these borders from continuing or developing various kinds of relations despite the existence of such new political boundaries. Thus the need to again return in this brief study to the significance of unrecorded transborder trade and economic relations between African countries in the post independence era.

2. Trade is one essential element that independent Africa's pursue in strengthening their interdependence and also as a means of economic cooperation. Intra-African trade existed long before the advent of colonialism in the continent. The only difference is that it was neither formalistic nor carried out through legally established channels as is the case at present. After independence, more attention has been paid to developing this trade despite the decline in its recorded trend of growth. However, unrecorded is not by any means synomymous with illegal trade. It takes place across official borders but less through accepted crossing points of many African countries. Although unrecorded trade cannot be properly assessed, it is large enough to be of concern to countries affected by it. It is in the light of some of these developments that African countries were prompted, and requested, the United Nations Economic Commission for Africa (ECA) secretariat to undertake studies on transactions in this area with a view to establishing the extent to which this type of activity contribute the region's overall trade volume and draw lessons for other sectors of the economy.

3. This report therefore highlights the situation of unrecorded trade as it is actually taking place in many African countries. Its contents are to a very large extent also based upon previous desk studies which have been carried out by the secretariat.

It is for this reason among others that the study attempts to focus attention on the following main issues: the different forms of border trade, the main types of products which are dealt with in these transactions, the factors responsible for unrecorded border trade; and its economic impact on African economies, especially in the informal sector. It also contains recommendations for consideration with a view to overcoming some of the problems addressed.

II. DIFFERENT FORMS OF UN-RECORDED BORDER TRADE

4. Although no systematic information is available, the widespread unrecorded trade practices in many parts of Africa range from physical smuggling of goods, theft, falsification or forgery of trade documents, faulty recording of goods or under-and over-valuation of goods for the purpose of evasion of customs duties, traditional market places and transit trade.

(a) Smuggling

5. Among the various illegal trade practices, smuggling consitutes one of the most severe concerns for African countries. It can be defined as the use of illegal channels of movements of goods across national boundaries and illegal traffic in currencies. Physical smuggling is operated, in most cases, on an organized basis. With the complicity of suppliers and buyers on border areas, organized individuals purchase goods in sufficient quantities to ferry across unpatrolled territory. This operation is sometimes facilitated by the fact

that people of the same ethnic origin, inhabit border areas where smuggling takes place. Payment for these trade transactions is made in one of the currencies of the two border countries. Since the currencies of many African states are not officially convertible, the exchange rate for these transactions is determined by supply and demand of these currencies available for such trade. This exchange rate may differ from the official one in case of convertibility of national currencies. The differential between the official and parallel or black market exchange rates tend to be larger when controls in one country are more stricter than in an other. The prevalence of parallel markets in some African countries also facilitates smuggling for border trade.

(b) Theft

6. This form of unrecorded border trade refers to transactions of goods, especially used goods which may have been stolen from a neighbouring country. Products which are involved in this category of border trade are the type that can yield attractive price and easy to dispose off such as used vehicles. Where the system has become semi-permanent dealers have also perfected the system of falsification of documentation.

(c) FAlsification and forgery of documentation

7. The falsification of documents consists of presenting false information regarding imported and exported goods through official channels. Where this is carried out on a large scale, this type of unrecorded trade has turned out to be a considerable source of losses in revenue to the concerned country. The forgery of documents is a serious malpractice and is very difficult to detect. Another problem created by forged documentations is the difficult it creates for customs officials so that even experienced and uncorrupted find it difficult to detect the genuine from the non genuine ones. This delays clearance and

creates suspicion on all traders and so dampers the enthuasism of bonefide traders to engage in transborder trade.

(d) Under-and over-valuation of goods

8. This practice aims at evading customs duties. It is performed through official channels at entry or exist points.

(e) Traditional market places

9. In many border villages or places there are periodic markets which are attended by populations on both sides of neighbouring countries. Traditional traders, who sale food crops and livestock products, are not familiar with modern techniques of international trade; they, instead, cross national borders to sale their products in these market places. .

(f) Transit trade

10. Experience shows that in some countries goods are smuggled into a country not within that country but are exported to other border areas in order to increase foreign exchange earnings not necessary for the country but the individuals concern. Transactions through this kind of system has tended to include products such as coffee because of access to wider markets at the global level. At times, marketing boards of a neighbouring country unsuspectingly facilitates this trade transaction, especially where smuggling into areas that do not grow or produce the crop in question in great quality.

III. STRUCTURE AND COMPOSITION OF COMMODITIES TRADE AT THE BORDERS

11. As briefly mentioned in the introduction, people in Africa that live across common borders traded among themselves even before the former colonial powers set up the current formal boundaries that separate them into different countries. The commodities mostly traded at borders consist of food and some other consumer goods and are a reflection of the demand for these products. It is also recognition of the fact that traders respond to people's basic needs. Categorized under the United Nations Standard International Trade Classification (SITC), the main products which fall under border trade are:

(a) SITC Section 0: Food and Live animals: wheat, maize, rice, tomatoes, potatoes, corn, millet, sorghm, beans, peas, cassava, groundnut, bananas, fruits; fish, sheep, goats, cows, different kind of meat, coffee and tea. A large portion of these goods crosses the borders to feed traditional border markets;

(b) SITC Section 1: Beverage and tobacco: beer, wine, spirits like whisky and gin, tobacco leave, cigars and cigarattes and soft drinks;

(c) SITC Section 6: Manufactured goods: soap, radios, ready made shoes and clothes, rubber tyres, matches, toilet papers, cement and other building materials. Imported manufactured goods also predominate among the commodities traded at the borders;

(d) SITC Section 2: Crude materials: hides and skins, natural rubber, timber, crude minerals such as crude gold and precious stones; although a large part is officially exported. The transaction in some of these products are paid for in convertible foreign currency.

IV. MAIN CAUSES FOR UNRECORDED TRANSBORDER TRADE

12. It is easy to understand in the light of the above why trade operators at border tend to be merely motivated by the need to respond to basic needs of people living accross the borders. Over the years, unrecorded border trade has expanded as a result of a number of reasons. For instance:

(d) The Profit motive

13. The fact that many African countries are unable to effectively patrol all their respective boundaries, encourages certain enterprising businessmen to take advantage of the opportunity created by smuggling of goods that meet immediate consumption domestically or re-export. These opportunities also help the businessmen, involved in such trade, to increase their profits by avoiding the payment of taxes and duties on goods traded at uncontrolled transborders.

(b) Similarity of ethnic population at common borders

14. When former colonial powers drew up the political boundaries dividing African countries, they happened to separate people who share a common language and culture. Illustrative examples include: the Ghana/Togo border at Alfao, the Nigeria/Benin border and the Tanzania and Kenya border where single ethnic populations overlap national boundaries. These are points where official border posts exist but unrecorded trade goes on almost infull need for the very reason of common ethnic loyalty. As a result, border populations continue their trading and transactions by ignoring the rules and procedures of international political boundaries.

(c) Proximity of settlements to borders

15. Along with the separation of some ethnic population at borders, proximity of settlements to borders creates difficulties in controlling the movement of goods. Indeed, some parts of African countries are so distant from the capitals which encompass regular markets and from the main centres of production but close enough to those of neighbouring countries to make border trade inevitable for inhabitants of these areas. Goods originating from both sides of neighbouring States are freely traded at the borders.

(d) Tariffs and other restrictions

16. In free trade transactions, goods would normally cross national boundaries without any restrictions and there would not be motivation for smuggling. Trade and tariff policies of African countries generally tend to protect infant industries from industrialized countries and to increase government revenue. Data show that intra-African tariffs and customs duties are very high. Furthermore, other non-tariff barriers such as import prohibition, health regulations, quotas and licencing on the import or export considerably limit the volume of recorded intra-African trade. The imposition of high tariff and complex non-tariff barriers in international trade transactions generally create incentives for business enterprise to engage in smuggling trade across borders. The higher the level of tariffs and the more complicated trade restrictions, the greater will be the desire to smuggle. Profits are reduced by high tariff on legal trade transactions. Smuggling therefore becomes an alternative to easing this situation.

17. As they are applied in many African countries, administrative procedures can be regarded as trade restrictions which could easily motivate trade operators

to smuggle. In many African countries, imports or exports are subjected to licences which have to be obtained in advance from authorizing departments. Such procedures are often cumbersome and time consuming. Such difficulties discourage trade operators who then resort to smuggling.

(c) Disparity in currency values and exchange rates

18. Except for a few African States that operate limited or linked to convertible currency systems like the CFA franc, most African countries have their own currencies which are not easily convertible. Currencies of these African are unofficially bought and exchanged at common borders. These deals are not aligned with the official exchanges rates. These paralled or "black" market operations exist in spite of national currency regulations. When a currency is weak or over-evaluated vis-a-vis others trade operators in weak currency areas take the opportunity to earn the stronger currency of the neighbouring country because it increases their purchasing power. It is also encourages holders of the stronger currency to acquire the weak currency at discounted rates since it makes the products expressed in the weak currency relatively cheap.

(d) Shortages of foreign exchange

19. Many African countries have been experiencing shortages of foreign exchange and have had to impose strict control on allocation of foreign exchange. In the light of these regulations, some traders then resort to smuggling goods into neighbouring States in order to be able to obtain hard currencies from unofficial currency dealers. These acts are more prevelent when the

(e) Price differentials and shortage of commodities

20. Producer prices vary from country to country. In many African countries, farmers are obliged to sell their cash crops to government marketing boards which fix producer prices, generally lower than the level that obtains for international prices. When prices at borders are high, traders get the incentive to smuggle. Differences in government tariff and fiscal policies on products as well as the cost of transport to the borders are some of the elements that account for prices differentials for similar goods on both sides of the border.

21. Import restrictions, such as prohibition, do create a shortage of some goods which in turn attract illegal trade in these scarse commodities apart from increasing their prices.

V. IMPACT OF UNRECORDED TRANSBORDER TRADE

22. The unrecorded transborder transactions have a number of economic implications for countries affected by such trade. Many of these implications can be summarized to include the following:

(a) Loss of revenue

23. The imposition of import taxes or export duties and such other charges stamps, administrative, statistical or storage fees at official borders on

international trade transactions are said to be responsible for the growth of unrecorded trade. It is obvious that goods which are illegally exported or imported escape taxation both as imports and exports. Since many African countries derive a large proportion of their public finances from customs duties and equivalent taxes, wide-spread smuggling constitutes a considerable loss of revenue. Indeed, revenue losses from unrecorded border trade is quite difficult to estimate, but, given the fact that unrecorded transborder trade is no longer confined to traditional exchange of basic goods and services between inhabitants sharing common border, its spread to products and commodities for resale in urban areas or for re-export, indicates the magnitude of government revenues lost as a result of these illegal transactions.

(b) Foreign exchange leakages

24. Another important aspect of smuggling of goods on exporting countries is the adverse effects of "leakage" it creates in foreign exchange. One category of this leakage relates to the illegal export of important products where a neighbouring country pays higher prices. Foreign exchange earned through smuggling is channelled into the parallel markets either to further finance smuggled goods or illegal financial transfers since none or little of these earnings are ever surrendered to Central Banks. The area of concern regarding the leakage in foreign exchange is that some of the smuggled goods may have

been originally imported for internal consumption and paid for in foreign exchange. A major impact of these leakages is the reduction in the local monetization of governments' foreign exchange. Combined with government revenue losses resulting from illegal trade transactions, these leakages considerably decrease public investment ability. They reduce the share of investment in the informal sector where development inputs are greatly needed. Negative consequences of these leakages on affected African countries include heightening the external debt and their inability to meet investment needs, as well as coping with the position of balance of payments.

(c) Shortages of goods

25. Higher demand and attractive prices in neighbouring countries create incentives for traders motivated by high profits to engage in the smuggling of large quantities of goods. Two consequences are to be highlighted: (i) as in the earlier example, the exporting country will suffer from shortage of most of its goods as smuggling increases. Consumers will therefore be obliged to pay higher price for some imported goods; (ii) the importing country will face unfair competition due to cheaper prices of smuggled imports which are not taxed and can therefore easily compete with the locally produced goods. As a result, the local industry will face low demand for its products and is forced to reduce its manpower to cope with the situation. On the other hand, the exporting industry will take advantage of this new market to expand its production an activity which in turn leads to creating employment opportunities.

(d) Improvement of livelihood

26. The analysis in the preceeding section shows briefly the impact that smuggling of goods can have on industries which produce goods that feature prominently in that practice. This paragraph suggests that unrecorded border trade, which is an integral part of unrecorded economic activities does have certain positive effects on the welfare of individuals who are involved in the transaction and other sectors of the economy. The profit that these businessmen make by using unauthorized border crossings would have been used for other productive purposes, especially where such trade takes place through normal channels and the required duties are paid indirectly by those in the formal sector.

(i) Farmers: Farming (agriculture livestock) accounts for the greatest proportion of the labour force engaged in the informal sector. Farmers sell crops to both official and unofficial markets. Although data on their incomes derived from parallel markets are unavailable, it is still possible to assume that an increase in smuggling of food crops for reasons which were identified earlier, there will be a corresponding increase in food production and rural household income.

(ii) Traders: Employment in the informal sector generally employ women because they are easly accessible. A large proportion of the female population is engaged in informal trade. Smuggled goods thus constitute an important source of supply and when these illegal transactions increase, the number of intermediairies as well as the small markets for smuggled goods also increases.

(iii) Transporters: It is generally admitted that smugglers purchase goods in sufficiently large quantities and hire porters to carry the goods in small quantities across unpatrolled boundaries, usually at night time. Small lorries or taxis are also used in smuggling, depending on the nature of goods involved. It is evident that smuggling is successfully carried out at times with the tacit understanding of the farmers who are the suppliers and the consumers/buyers on the other side of the border. Transporters derive substantive incomes from the unrecorded transborder trade.

(iv) Measures to control unrecorded border trade

27. There is no dobut that many African countries have, since their independence, attempted to institute a number of anti-smuggling measures with a view to alleviating the negative effects of the illegal trade practices. However, there are considerable difficulties as experience has shown regarding quantifying as is controlling of unrecorded trade across borders because the main root causes are quite varied. Nonetheless, the following measures continue to be used to cope with this problem:

(a) Administrative measures

28. Many African countries concentrate their control efforts on official borders, due to insufficiency of both human and financial resources. As indicated, smuggling is successfully operated because most African countries have extensive boundaries that extend thousands of kilometers. However, certain countries have paid sufficient attention to the situation by reinforcing border patrol.

29. In many African countries, institutional measures have been taken by developing the efficiency of the department of customs. Some countries have even established anti-smuggling committees or task forces as well as trained anti-smuggling squads and equipped them with modern equipment to enable them detect and prevent the prevalence of unrecoded transactions. It is obvious that a very well-organized customs office would overcome smuggling, especially at official borders. Another aspect of efficient anti-smuggling campaign is a constant supervision of staff posted at the borders. It is not enough to train officials and post them at different borders, but it is important to have constant guidance and supervision from headquarters in order to increase their efficiency and maintain their integrity with a view to avoiding corruption which could boost smuggling.

30. It is also advisable to increase raids on customs stations, in traditional markets and in border shops to assertain the existence of contraband goods. Once the smugglers are apprehended, it is important that they should be brought before the courts and judged according to existing laws and ensure that those contemplating similar activities should feel discouraged..

(b) Economic measures

31. As earlier pointed out, high tariff and non-tariff protective measures create some of the incentives that whet the appetite of traders involved in smuggling to continue. To reverse this trend, some African countries reduce excise duty on some products sensitive to smuggling, while others have also granted subvention to pioneer industries which were likely to suffer from unfair competition due to smuggling.

32. It should be recalled that complex trade procedures in attaining import or export licences have been mentioned as one of the elements that sustain illegal trade transactions. The main difficulties that may result in some cases would be the inability of semi-literate traders to cope with these cumbersome formalities. One of the solutions to this problem could be the issuance of trade licences or simplification and harmonization of trade documentation by concerned authorities where border trade is a major problem.

33. As a way of tackling smuggling caused by price differentials, some African countries undertook to liberalize prices in order to discourage smuggling of goods into neighbouring countries. This measure has proved to be successful in cases where there are proper implementation and follow-up mechanisms.

34. Other countries undertook monetary measures to encourage exports and combat smuggling and black marketeering. The laws and instrument utilized in cases of this kind include devaluation of national currencies vis-a-vis such hard currencies like the United States dollar. However even in cases of this kind the extent to which the system has been contained still leaves much to be deserved.

(c) Bilateral customs co-operation

35. In certain other instances, joint Border Commissions between neighbouring countries have been set up in some African countries to review border trade issues. Other countries on the other hand have concluded bilateral trade agreements identifying products that are allowed to be freely traded in order to combat smuggling. Co-operation between customs administrations has also been found to be an efficient means of controlling illegal trade transactions. It is sometimes found that border customs officials are responsible for facilitating smuggling of goods into their respective countries while where

such cooperation exists, this trend does not exist. This is why there is a strong case for neighbouring countries to strengthen co-operation among customs officials.

VII. CONCLUSIONS AND RECOMMENDATIONS

A. Conclusions

36. Available data show that the level of registered intra-African trade is very low, representing around 5 per cent of total Africa's trade. This brief study has attempted to confirm that a significant part of unrecorded intra-African trade takes place at national boundaries. Because of unavailability of quantifiable data, the magnitude of this type of trade is not easy to establish but this does not imply that its existence can not be proved beyond doubt.

37. Findings in this study and the ones before, explain the major factors responsible for unrecorded border trade. These include: (a) such physical obstacles as extensive border land areas which make it difficult for governments to police effectively; (b) the prevalence of high tariff and non tariff barriers; (c) the disparity in local currency values and the shortage of foreign exchange; (d) the lack of co-operation between customs officials; and (e) demand for goods which can not be produced locally.

38. Unrecorded border trade has certain negative impact on both countries. For instance revenue losses and the leakages in foreign exchanges is not only for countries from which the goods are exported but also those who are importers. Although the degree of the impact varies from one country to another, the losses incurred by some countries can be quite considerable.

39. Some African countries undertook measures to reduce or eliminate these effects from the point of view of illegal trade practices. These measures include such administrative action as the formation of smuggling squads, anti-smuggling operations, intensification of border patrols; economic measures in terms of price liberalization and fiscal alleviation as well as customs co-operation on bilateral basis.

B. Recommendations

40. The following recommendations are proposed on the basis of some of the causes and effects analysed as contained in this study:

(i) In order to curtail illegal transborder trade, governments should promote investment and provide incentives to increase the production of food and essential commodities to satisfy internal demand;

(ii) Governments should adopt appropriate pricing policies for agricultural and mineral products to encourage producers to maintain production and sell through official marketing channels;

(iii) Marketing boards and co-operative systems should be streamlined and made more efficient in the collection of goods and timely payment to producers;

(iv) Transport networks and storage facilities should be improved to facilitate internal management of agricultural production;

(v) Measures should be taken to remove wide price differentials with neighbouring countries in the pricing of food, essential commodities as well as luxury consumer goods;

(vi) The level of import duties and export taxes should be adjusted so as to remove the temptation of tax evasion as an incentive to smuggling. Where feasible, tariff and customs rules and regulations should be harmonized with those of neighbouring countries;

(vii) Decentralize trade licencing system to border areas in order to encourage traders resident in those areas to use official trade channels;

(viii) Where possible, liberalize foreign exchange allocations and control to allow easier imports of essential goods;

(ix) Undertake regular reviews of official exchange rates with currencies of neighbouring countries and institute a system of settlement of trade transactions in these currencies;

(x) Where the currency of the country was unstable, a system of dual exchange rates could be considered to level off the supply and demand of hard currencies;

(xi) Customs administration should be improved by providing adequate facilities to customs officials to carry out their functions efficiently and effectively;

(xii) Joint Border Commissions should be encouraged and strengthened and made to meet regularly;

(xiii) Introduce more punitive measures to discourage smuggling;

(xiv) Take appropriate measures to facilitate trade which is presently taking place illegally;

(xv) The number of border posts should be increased and the existing ones should be strengthened.